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SENSITIVE
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MCC FOR MBOHN, SRHODES, SGAULL, MTEJADA

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TAGS: EAID ECON PREL PGOV CO
SUBJECT: MCC MEETS WITH CROSS SECTION OF COLOMBIANS ON
FACT-FINDING VISIT MAY 17-23

¶1. (U) SUMMARY. During its initial visit to Colombia, a delegation from the Millennium Challenge Corporation (MCC) explained the organization's mission and procedures to Colombian Government, civil society, and business communities. The delegation's interlocutors in Bogota and Cali identified inadequate transport infrastructure, inefficient economic policies, and institutional issues as significant impediments to economic growth in Colombia. Tension between decentralization/centralization regarding public investment was an additional challenge that came up. The Colombians showed receptivity and enthusiasm to MCC's message, while remaining realistic about the time that it will take to arrive at an eventual compact. The GOC committed to forming an interagency team that will work full time to analyze constraints to growth, hiring a National Program Coordinator to lead the team, defining a public consultation strategy, and developing a work plan, in close collaboration with MCC. The GOC also indicated that the National Planning Department would take responsibility for following up on Colombia's performance on the MCC indicators. END SUMMARY.

¶2. (U) The MCC delegation included Chief of Staff Matthew Bohn, Development Managing Director Stacy Rhodes, Senior Director Stephen Gaull, and Program Analyst Monica Tejada. During the May 17-23 visit, they met with GOC (MFA, Presidential social welfare agency (Accion Social), Finance Ministry, and National Planning Department) officials, local governments, NGOs, USAID beneficiaries, academics, multilateral development banks, and business organizations and leaders.

MCC REACHES OUT TO STAKEHOLDERS

¶3. (U) The purpose of MCC's visit was four-fold. First, the delegation presented to stakeholders the implications of the December 2008 MCC Board decision that Colombia is eligible for MCC program assistance. Second, the delegation stressed the importance of managing expectations with respect to potential size and timing of a compact, as well as the need to de-politicize the compact development process. Third, the delegation listened to diverse viewpoints on constraints to economic growth in Colombia. Fourth, the delegation sought to sensitize the GOC to MCC's mandate of reducing poverty through growth. Accordingly, the delegation explained that it would be difficult for MCC to support the sort of social assistance programs that figure prominently in Accion Social's mandate, on which President Uribe places a political

priority.

¶4. (U) The delegation noted that Colombia must continue to score in the top 50th percentile of the Control of Corruption indicator as well as at least one-half of the indicators in each of the three policy categories (Ruling Justly; Investing in People; and Economic Freedom) to remain eligible for MCC assistance. The team then laid out the process by which a country must conduct meaningful public consultations before defining a compact proposal based on a formal analysis of constraints to growth. They pointed out that Colombia, as a lower middle income candidate, would have any compact capped at 25 percent of the MCC fiscal year's appropriated funds. The delegation also made clear to its Colombian partners that any compact could not be signed until FY 2011, given the time necessary to develop the proposal and MCC's other prior commitments of FY2009-2010 funding.

¶5. (U) The delegation mentioned that MCC would seek to harmonize its efforts with the International Cooperation Strategy (a tri-partite agreement between GOC, donors, and civil society) and with other national development initiatives of the GOC. MCC also noted that it would seek to collaborate operationally with other development partners, such as the World Bank and the International Finance Corporation, which are investing $1 billion and $100 million per year, respectively, in Colombia. MCC expressed a desire to work closely with the Embassy to complement existing foreign assistance activities, including the proposed Colombia Strategic Development Initiative (CSDI). Similarly, the MCC team noted the value of working with the private

sector to mobilize additional sources of capital, particularly given Colombia's relative sophistication and enabling environment for public-private partnerships. The delegation explained MCC's comparative advantage in scaling up or replicating existing projects that meet the criteria of reducing poverty through growth.

INFRASTRUCTURE MENTIONED REPEATEDLY AS MAJOR IMPEDIMENT
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¶6. (SBU) In virtually all of their meetings, MCC heard how internal transport infrastructure (primarily roads) suffered from systemic underinvestment and represented a significant brake on Colombia's economic potential. Competitiveness was a major recurrent theme stakeholders stressed, and one that experts have analyzed extensively at the national and regional levels. Chamber of Infrastructure President Juan Martin Caicedo noted some advances on infrastructure over the last 10 years as the GOC has accepted the use of concessions. However, he argued that numerous institutional problems, including weaknesses in the Ministry of Transport and the lack of an independent regulator in the transportation sector, continue to result in low public sector budget execution and to discourage private investment. While some major highway projects are proceeding, such as the "Route of the Sun" from Bogota to Santa Marta, improvements in secondary and tertiary roads linking rural areas to markets -- an essential to combating rural poverty -- are lagging.

¶7. (U) Business leaders from Cali and Buenaventura noted the tremendous geographical advantage that Colombia has as the only South American country with Pacific and Caribbean coasts, and pointed to the growth potential associated with port complements, such as industrial parks and interior ports. Representatives of multilateral lending institutions pointed out that Colombia lacks a facility to provide guarantees and credit enhancements for major project investments, unlike many other countries. Such a facility could play an important role in mobilizing greater participation by local financial institutions and pension funds in infrastructure finance. Institutional investors have been reluctant to invest in infrastructure, because of inadequately structured projects and changing rules of the

game.

ECONOMIC POLICY IMPROVEMENTS OFFER GROWTH POTENTIAL
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¶8. (U) Other interlocutors asserted that incoherent and inefficient government policies represented greater bottlenecks to growth than physical infrastructure. Several pointed to the fact that freight rates are not set by the market, but instead dictated by the government under political pressure from truckers. Similarly, high taxes on gasoline and new trucks translate into uncompetitive transport costs. International business consultant Martin Gustavo Ibarra opined that domestic logistics costs are three times greater than elsewhere in Latin America, representing a 12-14 percentage point premium on the cost of doing business in Colombia. He added that reducing such costs is more important to Colombia's competitiveness than a free trade agreement with the U.S.

¶9. (U) A group of noted Colombian economists identified several policies that limit Colombia's competitiveness and potential for economic growth. Among them were tax loopholes; high non-salary benefits formal employers are required to pay; subsidies for well-established agro-industries, such as sugar and flowers; and a system of incentives that keeps families on welfare. They all pointed to limits on land access because of informality and ambiguity in land titling as an impediment to economic growth. Several participants noted that limited access to education results in low investment in poor areas because of a lack of human capital. They also pointed to inefficient economic (but politically popular) public spending focused on consumption as opposed to investment.

"HIGHLY CENTRALIZED" SYSTEM PRESENTS CHALLENGES
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¶10. (SBU) The MCC delegation heard several complaints about the tensions between decentralization, as outlined in the Constitution of 1991, and a high degree of centralization in Colombia, which has the potential to affect MCC activities. Roberto Steiner, President of think tank Fedesarrollo, opined that the "community councils" that President Uribe hosts throughout the country and give citizens the opportunity to raise issues with the President and his cabinet have had a detrimental effect on Colombian democracy. "Community councils focus the national government's attention on local potholes instead of national highways, while absolving local leaders of accountability for issues the central government has now usurped," argued Steiner. Moreover, local governments have little incentive to raise their own sources of revenue. Other interlocutors noted that national-level institutions have been captured by political interests. Amunafro, an association of 92 municipalities with Afro-Colombian populations (where poverty is concentrated), argued that the central government did not have an accurate sense of the situation in the countryside and rarely listened to the regions. For this reason, they urged MCC to continue direct communications with entities other than the GOC. Similarly, NGOs expressed mistrust of the GOC and any consultative process they could put together.

NEXT STEPS: NAMING A TEAM AND DEFINING CONSULTATION MECHANISM
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¶11. (U) During outbriefs with the GOC and the Ambassador, the MCC delegation laid out next steps for Colombia. First, the GOC will name a team to work full time on the compact proposal. The GOC indicated the team would have representatives from Accion Social, the Department of National Planning, and the Ministry of Finance. The GOC plans to hire someone from outside the government to lead the team. MCC extended an invitation to two team members to

attend the upcoming session of "MCC University" where they will have the chance to learn MCC procedures and practices in detail as well as interact with other countries working with MCC. Second, economists from MCC and the GOC will jointly conduct a desk study of the myriad national-level studies on constraints to growth, prior to the GOC's official submission to MCC of a constraints analysis. Third, the Colombian team will present to MCC its plan for conducting public consultations relating to use of compact funds. Finally, the Colombians will present a high-level outline of their proposal for potential compact assistance, which would eventually evolve into a draft business plan.

¶12. (U) The delegation encouraged the GOC to remain in contact with MCC to help guide and inform the process, in accordance with its regulations and procedures. The MCC team noted the need to focus the compact in order to achieve impact. This could include a regionally-focused compact in a country as large and diverse as Colombia, although a thematically oriented compact at a national level could also be possible. The Pacific coast region was mentioned several times as a prime candidate, given its high poverty rates, strategic location, and potential for economic growth. The Atlantic Coast was also mentioned frequently as an area that may be conducive to the sort of growth-oriented investments suited for MCC.

¶13. (U) The MCC delegation cleared this cable.
Brownfield